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No. 474

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Supreme Court of the United States.

OCTOBER TERM, 1942.

HELEN SEARS BRADLEY ET AL.,
Petitioners,

v.

WILLIAM M. WELCH, FORMER COLLECTOR,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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Supreme Court of the United States.

OCTOBER TERM, 1942.

HELEN SEARS BRADLEY ET AL.,
Petitioners,

v.

WILLIAM M. WELCH, FORMER COLLECTOR,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

The undersigned, on behalf of the above-named petitioners, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the First Circuit entered on July 24, 1942, in the case between the parties docketed therein as No. 3772.

Opinions Below.

The opinion of the United States District Court for the District of Massachusetts (R. 87-100) is reported in 37 F.S. 788. The opinion of the Circuit Court of Appeals (R. 157-169) is reported in 130 F. (2d) 109.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered July 24, 1942 (R. 169).

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

The Question Presented

This case involves the proper rate of depreciation upon business real estate held by a family real estate trust, under which a mother and daughter enjoyed respectively two-thirds and one-third of the net income. Prior to 1920 they had owned the property as tenants in common in the above proportions. Under the trust they became equitable owners in the same proportions. The Commissioner contended and the court held that if this was a revocable trust under Section 166 of the Revenue Acts of 1932 and 1934 the basis of depreciation was the value of the buildings on March 1, 1913, plus the cost of improvements between 1913 and 1920. It is undisputed that unless it was a revocable trust under Section 166 the basis of depreciation was the fair market value of the buildings on December 31, 1920, the date of acquisition by the trust. We do not press our contention below that if Section 166 governed the Commissioner applied the wrong basis of depreciation. That is a question of no public importance. But we petition on the ground that the trust was not a "revocable trust" under Section 166. Upon this point the court's decision is of great moment and public importance, for it is opposed to the clear distinction, always recognized by this Court, and by every other court, between a trust which may be revoked by the grantor alone or with the consent of a compliant person, and a trust which stands unless terminated by

agreement among the persons who before the trust was formed were the real owners of the trust property.

Upon this exact point there is no conflict among the Circuits, for the point never arose before. The decision is unique and is due to the court's misconception of the meaning of the recent opinions of this Court of which *Helvering* v. *Clifford,* 309 U.S. 331, is an example. It would result from the decision, if followed, that every family real estate trust where the members of the family were not "at loggerheads" (Magruder, J.), though irrevocable except by joint action of the beneficial owners, would be a revocable trust within the meaning of Section 166, unless each beneficial owner has a "substantial pecuniary motive" (Magruder, J.) for opposing revocation.

Our point is that Section 166 applies to a trust set up by "*the* grantor", who reserves power to take back the property in whole or in part by assent of a person not having a substantial adverse interest, but that it does not apply to a genuine trust created by joint owners of property, whether they are mutually agreeable members of a family or not, and whether the pecuniary interest of one is substantial or not. The latter situation does not call for a "realistic appraisal" (Magruder, J.). Each beneficiary of such a trust has an absolute right to refuse to become again a tenant in common of the property whether or not he can point to any special advantage to himself from the trust rather than from a tenancy in common.

Section 166 follows:

> "SEC. 166. REVOCABLE TRUSTS.
>
> Where at any time . . . the power to revest in the grantor title to any part of the corpus of the trust is vested—
>
> (1) in the grantor, either alone or in conjunction with any person not having a substantial adverse in-

terest in the disposition of such part of the corpus or the income therefrom, or

(2) in any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom,

then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor."

The trust could be terminated or modified during the joint lives of the two beneficiaries upon their joint written request to the trustee. After the death of either the trust could be terminated or modified by the written request of the survivor.

The trust was in existence during the years involved, 1932 to 1935. The mother died on September 26, 1935.

Specification of Errors.

The Circuit Court of Appeals erred in holding that the trust was a revocable trust within the meaning of Section 166 of the Revenue Acts of 1932 and 1934.

Reasons for Granting the Writ.

The court failed to distinguish between a trust created to route a grantor's income among his family, and which is substantially revocable at his pleasure, and a genuine trust created by owners of property. The court employed a wrong test to decide whether the former tenants in common or owners in severalty possessed substantially adverse interests to each other. The court misapplied to the latter sort of trust the criteria established by this Court for the former sort of trust.

Section 166 is directed solely against avoidance of income tax. It is not intended to declare revocable every family trust where the beneficial owners are agreeably disposed to each other and where they cannot point to a specific pecuniary advantage from the continued existence of the trust.

Wherefore, it is respectfully submitted that the petition should be granted.

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Supreme Court of the United States.

OCTOBER TERM, 1942.

HELEN SEARS BRADLEY ET AL.,
Petitioners,

v.

WILLIAM M. WELCH, FORMER COLLECTOR,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

The distinction between an illusory trust by which "the grantor" re-routes his own income from his own property among his family group, and a trust where tenants in common establish a trust of their several properties, is well illustrated by an opinion of the Committee on Appeals and Review in 1921, before Section 166 had been enacted—5 C.B. (1921), p. 184.

The heirs of an intestate had joined in the creation of a trust of their inheritance which was irrevocable except by joint consent. The opinion was:

> "The trust instrument in this case is revocable, but it must be remembered that the action of all the grantors must coincide. It is not possible for any one

> of them by his own act to repossess himself of the property and assert the complete ownership and control of his portion of it, as is true in the case where there is but a single grantor. He must persuade all of the other grantors—who in this case are also beneficiaries under the trust instrument and might be adversely affected by such revocation or amendment—to consent to the revocation. . . . Since, therefore, it is impossible for any one of the grantors to assert ownership over his portion of the property by his own act, it seems wrong in principle to tax him individually on the income from that portion of the property on the authority of a regulation which has ownership as its basis. It is concluded that the income from the A estate trust in so far as it is to be accumulated should not be taxed to the grantors."

To hold, as the Circuit Court does, that such a trust is revocable at the will of any one of the grantors, if they are a friendly family, because the power to persuade the others enjoyed by each of the friendly grantors is a "power to revest" under Section 166, unless the others have a "substantial adverse interest" in the sense of a personal special or hostile interest not enjoyed by each of the others reciprocally, would lead inevitably to the destruction of genuine family trusts.

"Power to revest" under Section 166 means a power expressed in the trust instrument. It does not mean a power in one of the grantor-beneficiaries to control, intimidate, persuade or entice the others. Nobody before this case has ever suggested that it does.

The grantor-beneficiaries are the sole beneficiaries of the trust, enjoying the benefit of a single ownership of the legal titles instead of their former ownership in common.

The chance that one of them may persuade or coerce the other is not a "power to revest."

Section 166 by its very terms does not apply to this trust. It applies to "the grantor" who has "power to revest" in himself title to the corpus. It does not apply to two or more owners of property who put their property into a trust.

No decision before this one has suggested that if a court by "realistic appraisal" thinks that one of such grantors has such family ascendancy that the others will probably not oppose, the trust is revocable. Revocable by whom? Section 166 provides that it is revocable by "the grantor." Does this mean that it may be revoked by any one of the grantor-beneficiaries? If it requires that those who joined in granting also join in revoking, then it requires joint action of all, any one of whom may refuse for any reason whatever or for no reason at all. It is beside the point to suggest that no one may effectively refuse unless he can prove a substantial pecuniary interest in keeping the trust as it is.

In this respect the case is in conflict with

> *Stuart* v. *Commissioner,* 124 Fed. (2d) 772 (C.C.A. 7th),

which asserts the distinction between the recapture by the sole grantor of the corpus of the trust "by virtue of the future exercise of his influence" and its recapture by virtue of a power reserved in the trust instrument.

Evidently the court below was influenced by the remarks in *Helvering* v. *Clifford,* 309 U.S. 331, about "the normal consequences of family solidarity" and hence has assumed that the mother would have been able to persuade the daughter to terminate the trust, hence that the mother had "power to revest" her two-thirds in herself.

If we assume that the mother was dominant and could persuade the daughter to terminate the trust, then it must follow that the daughter was not dominant and would be unable to persuade her mother. It follows that the trust is revocable as to one grantor's share but not as to the other's.

The clear answer is that Section 166 has nothing to do with this trust.

Respectfully submitted,

FREDERICK H. NASH,
CLAUDE R. BRANCH,
JOHN DANE, JR.

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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 474

HELEN SEARS BRADLEY ET AL., PETITIONERS

v.

WILLIAM M. WELCH, FORMER COLLECTOR

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States District Court for the District of Massachusetts (R. 87–100) is reported in 37 F. Supp. 788. The opinion of the Circuit Court of Appeals (R. 156–167) is reported in 130 F. 2d 109.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered July 24, 1942 (R. 167), and the pe-

tition for a writ of certiorari was filed October 22, 1942. Jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended.

QUESTION PRESENTED

The taxpayers, mother and daughter, owned as tenants in common two-thirds and one-third interests respectively in real estate, which they conveyed in trust. Under the terms of the trust, the grantors retained their proportionate interests in the income during their joint lives and the power jointly to revest in themselves in the same proportions any part of the trust property. Each had the power to dispose of her proportionate share by will. In default of appointment by the mother, the daughter would receive the mother's two-thirds share if she survived; in default of appointment by the daughter, her one-third share would pass to her heirs.

The question is whether the income of the trust is taxable to the grantors under Section 166 (1) of the Revenue Acts of 1932 and 1934. The answer depends upon whether each of the grantors retained as to her respective share a power to revoke "in conjunction with" a "person not having a substantial adverse interest."

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. 10–12.

STATEMENT

In 1910 Sarah C. Sears acquired an undivided two-thirds interest and her daughter, Helen Sears Bradley, an undivided one-third interest in certain real estate. On December 31, 1920, by concurrent action, the property was conveyed to Mrs. Sears as trustee to manage the property and to divide the trust income between the grantors during their joint lives, two-thirds to Mrs. Sears and one-third to Mrs. Bradley. (R. 89.) The indenture contained the following provision for termination of the trust during their joint lives (R. 89):

> At any time during the joint lives of said Sarah C. Sears and said Helen Sears Bradley, upon the written request to the trustee or trustees hereunder signed and acknowledged by both the said Sarah C. Sears and said Helen Sears Bradley, this trust may be terminated as to any portion of the trust estate or as to the entire trust estate according to the terms of such request, and thereupon two-thirds of the trust estate or such portion thereof as is covered in such request shall be conveyed to the said Sarah C. Sears, and one-third thereof to the said Helen Sears Bradley, free and discharged of all trusts. * * *

The indenture further provided that upon the death of Mrs. Sears, two-thirds of the principal of the trust would pass to such persons and for such purposes as she should appoint by will. In de-

fault of appointment, and if Mrs. Bradley were still living, the entire estate would continue to be held in trust and the net income would be paid to Mrs. Bradley during her life; then, upon her death, the principal of the trust would pass as she should direct by will or, in default of such appointment, to the persons who would be entitled to the property if she had died possessed of it as her own. (R. 90.)

If Mrs. Bradley died first, one-third of the principal would pass to her appointees by will. If she failed to appoint, one-third would pass to the persons entitled to the property if she had died possessed of it as her own. The remaining two-thirds would be continued in trust, the net income to be paid to Mrs. Sears for life. Upon the death of Mrs. Sears, after Mrs. Bradley, the entire remaining principal of the trust would pass as Mrs. Sears should direct and appoint by will, or in default of appointment, to those persons who would be entitled to receive it if she had died possessed of the property as her own. (R. 91.)

The survivor was empowered at any time to terminate any portion of the trust that should continue. (R. 89–90.)

The Commissioner determined that the income of the trust for the years 1932 through September 26, 1935, was taxable to the grantors under Section 166 of the Revenue Acts of 1932 and 1934, and that therefore the basis for depreciation of the

trust property continued to be its basis in the hands of the grantors prior to the creation of the trust. (R. 45–46.) Refund suits were brought by the executors of Mrs. Sears and by Mrs. Bradley and tried together by stipulation. (R. 41.)

The District Court rendered judgments on behalf of the taxpayers (R. 51, 86–87), sustaining their contentions (1) that the income was not taxable to the grantors under Section 166, and (2) that even if Section 166 were applicable, the basis of the property was its market value at the date of acquisition by the trust under Section 113 (a) (4) of the Revenue Acts (R. 92–100).

The court below, on consolidated appeals (R. 155), reversed the District Court on both points (R. 167). The taxpayers seek review only of the first. (Pet. 2.)

ARGUMENT

1. Section 166 (1) of the Revenue Acts of 1932 and 1934 (Appendix, *infra*) provides that where the power to "revest in the grantor title to any part of the corpus" of a trust is vested "in the grantor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom," then "the income of such part of the trust * * * shall be included in computing the net income of the grantor." Under the terms of the trust indenture, Mrs. Sears and Mrs. Bradley ex-

pressly reserved the right by joint action to have any part or all of the trust property returned to them in two-thirds and one-third proportions corresponding to their original contributions. Each grantor, therefore, retained the power to revest in herself, in conjunction with the other, the portion of the corpus representing her original share of the trust property. The issue, therefore, is whether either party had a "substantial adverse interest" in the part of the corpus or the income which would thereby revert to the other.

Under the trust, Mrs. Bradley had a remainder interest in her mother's share, contingent upon survival, essentially equivalent to complete ownership. That interest, however, was dependent upon Mrs. Sears' failure to exercise the unrestricted power, which she held under the trust, to dispose of the property by will. Thus, Mrs. Bradley's chances of receiving the property under the trust were not materially greater than her chances of receiving it as her mother's heir if the trust were revoked.

To be sure, upon revocation Mrs. Sears could also dispose of the property *inter vivos*. But so long as Mrs. Sears retained the power to dispose of the property by will, Mrs. Bradley, from any practical standpoint, would not stand to gain by obstructing any wish her mother might have to dispose of it during her lifetime. Furthermore, as the court below pointed out, whatever slight pecu-

niary interest Mrs. Bradley might have in the continuance of the trust, would be offset by her pecuniary interest in its revocation, for she would also get back her one-third interest free and clear which thereafter she could convey to third parties in her lifetime.

Mrs. Sears' interest in continuing the trust, if Mrs. Bradley should wish to revoke it, was even more remote. Under the terms of the trust, Mrs. Sears' succession to her daughter's interest was dependent not only upon her daughter's failure to appoint but also upon the contingency that she should be her daughter's heir. Revocation of the trust certainly would not materially impair what slight hopes she might have of succeeding to the property. Clearly, she would not have a substantial pecuniary interest in opposing any wish of her daughter to revoke, particularly when at the same time she would regain complete control over her two-thirds interest.

There is no merit, moreover, in the contention that unity of ownership and management of the property in a trust, as distinguished from a holding by tenancy in common, established in either of the parties a substantial interest adverse to revocation. Each grantor's interests and powers paralleled the other's. There was no implication that complete harmony between them was lacking, or that "the normal consequences of family solidarity" were not to be anticipated. *Cf. Helvering* v.

Clifford, 309 U. S. 331, 337. In these circumstances it is unreasonable to suppose that either would find advantages in a continuance of the trust which would warrant a refusal to assent to revocation.

2. The petitioners contend that since Section 166 applies to the "grantor" who has "power to revest" in himself title to the corpus, it does not by its terms apply to two or more owners of property who put their property into a trust. (Br. 9.) Since this argument was not advanced in the court below, it may be questioned whether it is now available to the petitioners in seeking a reversal. *Cf. Helvering* v. *Wood,* 309 U. S. 344, 348–349; *Burnet* v. *Commonwealth Imp. Co.,* 287 U. S. 415, 418. But apart from this it is obvious that the construction urged would do violence to the plain meaning of the statute as applicable to *each grantor* of property to a trust. Furthermore, under a statute of long standing, "words importing the singular number" in federal enactments "may extend and be applied to several persons or things." Revised Statutes, Section 1 (U. S. C., Title 1, Sec. 1). It may well be argued that if the word "grantor" in Section 166 (1) is thus applied in the plural, the reservation of a joint power of revocation in joint grantors automatically brings the trust under that Section. Thus, the decision below may be supported on the alternative ground that, under the statute, it is unnecessary to inquire

whether or not either grantor had a substantial adverse interest.

3. The decision below is not, as the petitioners assert (Br. 9), in conflict with *Stuart* v. *Commissioner,* 124 F. 2d 772 (C. C. A. 7th), reversed, Nos. 48 and 49, present Term, November 16, 1942. In the *Stuart* cases trusts were involved in which the asserted power to revoke admittedly was not vested in the grantor himself; here the trust instrument expressly provided for termination upon the request of the grantors.

CONCLUSION

The case was decided correctly in the court below, and there is no conflict among the circuits. The petition for certiorari should be denied.

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NOVEMBER, 1942.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

* * * * *

(m) *Basis for Depreciation and Depletion.*—The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be as provided in section 114.

* * * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *

(4) *Gift or Transfer in Trust before January 1, 1921.*—If the property was acquired by gift or transfer in trust on or before December 31, 1920, the basis shall be the fair market value of such property at the time of such acquisition. * * *

* * * * *

(b) *Adjusted Basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

* * * * *

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(a) *Basis for Depreciation.*—The basis upon which exhaustion, wear and tear, and

obsolescence are to be allowed in respect of any property shall be the adjusted basis provided in section 113 (b) for the purpose of determining the gain or loss upon the sale or other disposition of such property.

* * * * *

SEC. 166. REVOCABLE TRUSTS.

Where at any time during the taxable year the power to revest in the grantor title to any part of the corpus of the trust is vested—

(1) in the grantor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom, * * *

* * * * *

then the income of such part of the trust for such taxable year shall be included in computing the net income of the grantor.

Revenue Act of 1934, c. 277, 48 Stat. 680:

Corresponding provisions of the 1934 Act are substantially the same, insofar as here material.

Treasury Regulations 77, promulgated under the Revenue Act of 1932:

ART. 881. *Income of trusts taxable to grantor.*—In the case of certain trusts which are in whole or in part subject to revocation by the grantor or by any person not having a substantial adverse interest, or which are for the benefit of the grantor, the income of the trust is to be included in computing the net income of the grantor. * * *

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 166–1 [as amended by T. D. 4629, XV–1 Cum. Bull. 140 (1936)] *Trusts, with*

respect to the corpus of which, the grantor is regarded as remaining in substance the owner.—

* * * * *

(b) Section 166 defines with particularity instances in which the grantor is regarded as in substance the owner of the corpus by reason of the fact that he has retained power to revest the corpus in himself. For the purposes of this article the grantor is deemed to have retained such power if he, or any person not having a substantial interest in the corpus or the income therefrom adverse to the grantor, or both, may cause the title to the corpus to revest in the grantor. * * *

* * * * *

(d) If the grantor is regarded as remaining in substance the owner of the corpus the gross income of such corpus shall be included in the gross income of the grantor, and he shall be allowed those deductions with respect to the corpus as he would have been entitled to had the trust not been created.

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